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VAT Protections: The Rest of the Story

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Report Highlights:

In order to promote certain sectors and because it is impractical for Chinese farmers to keep track of VAT-able transactions, the Ministry of Finance has implemented a variety of VAT exceptions. The following analysis finds that where the applied VAT is 13 percent on agricultural imports, the effective VAT on domestic products varies between 3.23 and 6.2 percent. While the effective VAT will vary depending on, among other things, market prices, profit margins and marketing costs, there appears to be a disparate impact on imports. Additionally, agricultural exports often receive a VAT-rebate valued at 13 percent, providing a form of export subsidy.

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Executive Summary

China, like many countries, relies on a value-added tax for tax revenues. In order to promote certain sectors and because it is impractical for Chinese farmers to keep track of VAT-able transactions, the Ministry of Finance has implemented a variety of exceptions. These include select farm inputs VAT-free, farm sales exempt from VAT, imputed VAT for products purchased from farmers, animal feed exempted from VAT, and imported product exempted from VAT, including animal feed. These are discussed below and Annexes 1-5 include detailed examples.

Except for the import product exemption, benefits accruing under these exceptions do not apply to imports. The impact is that there is an applied VAT and an effective VAT where the applied VAT is applicable to imports and the effective VAT is applicable to domestic products, adjusting for the VAT exceptions. The following analysis finds that where the applied VAT is 13 percent, the effective VAT on domestic products varies between 3.23 and 6.23 percent. While the effective VAT will vary depending on, among other things, market prices, profit margins and marketing costs, there is a disparate impact on imports, making these VAT exemptions inconsistent with the World Trade Organization's principles of "National Treatment."

Value-added Tax in China

In China, as in a large number of other countries, rather than charging a consumption or sales tax at the final point of sale, a value-added tax (VAT) is assessed at each transaction point. In the jargon of the tax code, this VAT shows up on the seller's receipt as a "sales VAT" and on the buyer's receipt as a "purchase VAT." The tax collector collects the difference between the "sales VAT" and the "purchase VAT" shown on business receipts.

However, China treats agricultural products differently than other products. The Ministry of Finance maintains several exemptions on agriculture both to promote certain sectors and because it is "impractical" for Chinese farmers, often poorly educated and with very small land holdings, to keep track of purchase and sales VAT.

Special Exemptions for Agriculture

Discussed below, exceptions to the value added tax (VAT) for the agricultural industry fall into five categories: farm inputs, farm sales, processor imputed VAT, processor exempted products, and import product exemption. Processor exceptions are either through an imputed VAT, or exempted products. Except for the import product exemption, benefits accruing under these exceptions do not apply to imports and are therefore probably inconsistent with the World Trade Organization's principles of "National Treatment."

The Cost to U.S. Competitiveness

The first three exemptions are tied together and are justified, from a policy perspective, because it is "impractical" for Chinese farmers, often poorly educated and with very small land holdings, to keep track of purchase and sales VAT. National Development and Reform Commission (NDRC) input/output data support the characterization of this as tax waiver not applied to imports.

The ratio of the value of material inputs (i.e. everything besides land, labor and taxes) to output value for major field crops in China, on average, is 1 to 3, or 33 percent. Corn has the highest ratio at 39 percent. (See Annex 4.) At least a quarter of these inputs, seed, pesticide, herbicide, agricultural machinery and some fertilizers, do not carry a VAT, however. Therefore, VAT-able inputs account for no more than 30 percent¹ of farm sales. At this rate,

¹ 39% (corn materials input ratio) x 75% (VAT-able inputs) = 29.25%

the purchase-VAT would be no more than 3.23 percent² (assuming a 13 percent³ VAT on inputs).

When the farmer sells the product, the sales-VAT is exempted and the purchaser imputes a 13 purchase-VAT which allows the purchaser to retain over 80 percent of the VAT as revenue and results in an effective rate of about 3.23 percent VAT, instead of 13 percent VAT applied to imports. In terms of the tax benefit, a grain dealer/trader that purchases grains from farmer, then sell the grains to feed mills, flourmills, crushers, or other processors will resemble an example of the grain trader in Annex 1.

Where the farmer sells directly to a processor or a state trading entity responsible for grain storage, these sales are also exempted from the VAT, passing this benefit down the distribution chain. See Annexes 1-5 for more details.

The Gang of Four Exemptions

Farm Inputs

Certain categories of farm inputs are exempt from VAT.⁴ Seed, pesticide, herbicide, agricultural machinery and some fertilizers, representing at least one quarter of inputs, are VAT-free, (but have an imputed VAT value of 13 percent when counting the purchase VAT.) On major Chinese field crops the ratio of the value of material inputs (i.e. everything besides land, labor and taxes) to output value is on average 1 to 3, or 33 percent.

Farm Sales

The following are considered VAT-free agricultural products: All products sold from agricultural producers.⁵ Agricultural producers are individuals or organizations handling agricultural production.⁶ Certain state trading enterprises, including state and provincial grain storage facilities, that buy from the farm and sell to primary processors, like feed or flour mills, are considered to be handling agricultural production. Others may associate with these state trading enterprises or operate in the black market, aggregating farm production and effectively acting as agents of the farmer.

Producer exceptions-imputed VAT

Buyers of products from farmers may claim 13 percent of these products' value as a purchase VAT. This exemption protects processors from paying the VAT that farmers are exempt from (and from double payment of VAT for farm inputs that were not VAT-free).

Producer exceptions-domestic feed

Sales of domestic feed products are VAT-free. This includes mixed feed, compound feed, premix feed, feed concentrate, bran, DDGS, oilseed meal (excluding soybean meal), fishmeal and bone meal. Domestic feed grains are exempt under the "farm sales" rule. Feed additives are subject to VAT. According to this policy feed mills and oilseed crushers

² 33% (average materials input ratio) x 75% (VAT-able inputs) x 13% (applied VAT) = 3.23%.

³ Purchase-VAT rates are 13, 17 or 35 percent, generally depending on whether the product is considered a basic product (food or production inputs), a consumable (clothes and appliances) or a luxury good (expensive automobiles).

⁴ State Administration of Taxation Notice (2001) No. 113 titled "VAT Exemption on Certain Categories of Agricultural Inputs"

⁵ 1993/1994 State Administration of Tax Regulation titled "The Temporary Regulation of the VAT," Article 16, Item 1 of the regulation, stipulates these products are VAT-free.

⁶ 1993/1994 State Administration of Tax Regulation titled "Implementation Procedures for the Temporary Regulation of VAT." Article 31 of the regulation, defines the agricultural producers

(excluding soy bean crusher) are VAT exempt. All other grain processors, including flourmills, starch manufacturers, and distillers do not receive a VAT exemption on their sale. While soymeal is not exempt from VAT, other oil meals are and crushers selling oil meal are not required to charge VAT or provide a VAT sales receipt.⁷

VAT Rebates on Exports

To promote exports, including agriculture-based exports, many are entitled to a VAT rebate. For many agricultural products the rebate is based on an indexed prices instead of market prices which can serve as an export subsidy. FAS/Beijing will address this issue in a subsequent GAIN report. Exclusive of indexing, because the VAT rebate is based on the applied VAT, the difference between the applied VAT and the effective VAT effectively is an export subsidy. Using the analysis in Annex 1 as an example, where the effective VAT is 3.23 or 5.8 percent, depending on whether the exporter buys from a farmer (or from government stocks), or from a commercial trader, the effective export subsidy is between 7.2 and 9.77 percent.

Import Exemptions

The following 15 imported feed ingredients are VAT-free. All other feed ingredients are (normally) subject to a 13 percent VAT.

List of VAT Exemption on the imported Feed Ingredients				
	HS Code	Commodity Name	VAT Rate	Applied VAT
1	23012010	Fish Meal	13%	0%
2	23012090	Other Aquatic Residue	13%	0%
3	23021000	Bran, Sharps and other Residue of Corn	13%	0%
4	23022000	Bran, Sharps, other Residue of Corn of Rice	13%	0%
5	23023000	Bran, Sharps, other Residue of Wheat	13%	0%
6	23024000	Other Grain Residue	13%	0%
7	23033000	Distiller's Dry Grain and Solubles	13%	0%
8	23050000	Peanut Meal	13%	0%
9	23061000	Cotton Seed Meal	13%	0%
10	23062000	Flax Seed Meal	13%	0%
11	23063000	Sun Flower Meal	13%	0%
12	24064000	Rapeseed Meal	13%	0%
13	23070000	Wine Lees	13%	0%
14	12141000	Alfalfa Meal, Pellet	13%	0%
15	12149000	Alfalfa, others	13%	0%

Annexes

Annex 1: Grain Trader

The following example illustrates how a VAT exemption for farmer sales and an imputed 13 percent VAT for farm product purchases, using a grain trader as an example, results in a lower VAT on domestic product than on imports.

A farmer sells a ton of corn to a trader for RMB 900. The transaction is not VAT-able, however the trader is granted an "imputed" purchase VAT. The farmer writes the trader a receipt for RMB 900, and this amount includes the imputed "actual price" of the corn, $900/1.13 = 796.5$, plus the "imputed purchase VAT", $796.5 \times 0.13 = 103.5$. These two sum together to the amount received by the farmer, $796.5 + 103.5 = 900$.

⁷ State Administration of Taxation Notice (2001) No. 30 stipulates that soybean meal, regardless imported or domestically produced is subject to 13% VAT. For other meals, either imported or domestically produced is free of VAT.

The trader in turn sells that grain for RMB 1,000 plus VAT to a feed mill and writes a receipt to the feed mill for RMB 1,000 plus a (13 percent x RMB 1,000) = RMB 130 VAT. Normally, since there is no purchase tax receipt, the trader would pay RMB 130 to the Tax Bureau. Instead, the trader can claim a "purchase VAT" equal to 13 percent of the corn value (the "actual price" above) and the trader pays a VAT of RMB 26.5 = RMB 130 - RMB 103.5 (0.13/1.13 x 900 RMB).⁸

The "imputed" purchase VAT overstates the actual VAT paid by farmers and evaluating the VAT paid by the farmer further illustrates the benefits of this tax treatment. Assuming a 33 percent ratio of input materials (i.e., everything besides land, labor and taxes) to output value, and that inputs are charged 13 percent VAT, this would mean that the actual VAT paid by farmers for field crops is at most (13 percent of 33 percent) 4.3 percent⁹ of the output value. In fact, Post estimate that approximately 25 percent of inputs to farmers are VAT-free¹⁰ making the effective VAT 3.2%. On this basis, the farmer actually paid RMB 29 VAT on inputs.¹¹

To compensate for farmers' VAT payments, traders should be allowed to claim at most a "purchase VAT" equal to 3.2 percent (RMB 29), not 13 percent, of the grain's value. The trader should pay a VAT of RMB 130 - RMB 29 or RMB 101.

The benefit to the trader is the difference between the VAT he should have paid and the VAT actually paid or RMB 101 - RMB 26.5 or RMB 74.5. Whether this benefit is actually retained by the trader or shared with the farmer depends on a variety of economic factors, but in all cases it prejudices imports. For the purposes of this report, the assumption is the purchaser retains the benefit.

The result in terms of the effective VAT tax is that instead of collecting the full RMB 130 or 13 percent as is assessed on imported corn delivered to millers or processors, only RMB 26.5 noted above, plus RMB 29 in VAT paid by the farmer. Thus, in this example, the effective tax is a little over 5.8 percent¹², not the 13 percent on the books.

Note that traders and processors that purchase directly from the local farmers (or a dealer that acts as farmer representative for VAT-collection purposes) often have to write their own receipt. Upon payment, because the farmer could not issue any legitimate receipt, the trader or processor will issue a receipt on farmer's behalf and keep a copy tracking the transaction on its accounting books.

⁸ VAT is usually deducted from the total price and is calculated using the formula = total price x .13 / 1.13 = VAT (at 13 percent). However, for the imputed purchase VAT on the sale by agricultural producers, the VAT formula = purchase price X .13. This is an additional 2.5% price benefit to domestic production. To illustrate: 13% of 900 = 117. Using the VAT rate formula 0.13/1.13 x 900 is 103.5 which is the equivalent to 11.5%. In practice, the 13% is actually assessed on the farmer sales prices so that formula is imputed purchase VAT = price * 13 percent. In this example, the imputed VAT would be 900 x .13 = 117. Thus, in practice, imputed purchase VAT is further overstated, further disadvantaging imports. For the purposes of this report, imputed purchase VAT will be assumed to be the 13 percent of the "actual price" or farmer sales price x .13/1.13.

⁹ 13% (VAT) x 33% (average materials input ratio) = 4.3%

¹⁰ Ministry of Finance and State Administration of Taxation (2001) No. 113 (See Annex 8 Regulatory References)

¹¹ RMB 900 x 3.217% = RMB 29.07.

¹² VAT Rate = VAT / (PRICE - VAT) = 55 (29 + 26 - farmer and trader VAT, respectively) / (1100 - 55) = 5.82%

Annex 2: Processors

Processors, whether feed or food millers, seed crushers, or ethanol or starch manufacturers fall into three categories in terms of input sourcing and two categories in terms of output tax regimes.

Input sources are either direct from the farmer, from affiliated traders, or from independent traders, though tax benefits provide incentives to purchase directly from farmers. Higher volume processors tend to have a greater number of arms length transactions. However, larger enterprises are more likely to have an affiliated trader that may provide an informal VAT rebate in exchange for capturing the maximum imputed VAT. Additionally, there is a wide network of small traders that consolidate farm production on behalf of the processor and are treated, for tax purposes, like farmers.

In these cases, the imputed VAT moves up the processing chain to processors. Factors that will affect the benefits to this program include:

- 1) When purchasing from the farmer, do the purchase receipts issued by the processor overstate the value paid to the farmer?
- 2) When purchasing from small traders, do such traders might act as a farmer representative and their practice will resemble a farmer?

Transactions by state and provincial enterprises, especially those involved in grain storage, are exempt from VAT when they buy from farmers and sell to processors or exporters. In the case of wheat, where 80 percent of the marketable wheat was purchased by state or provincial grain storage entities, this provides significant VAT exemption benefits. The benefit is less for corn and rice.

Insofar as processors are purchasing from farmers or farmer like sellers, their tax benefit will resemble the trader in Annex 1.

Food millers, ethanol and starch manufacturers produce VAT-able products. Food millers provide a 13 percent VAT sales receipt on output sold, and ethanol and starch manufacturers provide a 17 percent VAT sales receipt on output sold. Crushers have both VAT-able and non-VAT-able sales. Non-VAT-able products are all oilseed meal except soymeal. VAT-able products are soymeal and food oil, which are assessed a 13 percent VAT. Feed mills do not charge VAT on feed sold to producers.

Annex 3: Oilseed Crushers

The following analysis provides the estimated VAT on domestic oilseeds as compared with imported soybeans. Soybeans represent approximately 56 percent of total oilseed processing.¹³ Almost all non-soybean oilseeds are domestically sourced and approximately 25 percent of soybeans crushed are domestically sourced. The impact of VAT exemptions on oilseeds sourced domestically in China is consistent with Annex 1 and Annex 2. Imported oilseeds are assessed a 13 percent VAT on the CIF value plus duty.

Crushers' sales of non-soybean meal are not VAT-able. Sales of crude oilseed oil and soymeal are assessed a 13 percent VAT. Soybean processing is analyzed below.

A crusher purchases 1 MT of soybeans for RMB 2811. If the soybeans are imported, the crusher will receive a VAT purchase receipt of 13 percent of the purchase price or $2811 \times 0.13 / 1.13 = \text{RMB } 323$. If purchased from the farmer, the crusher will be able to take

¹³ Total oilseeds processed in MY 2006/7 are estimated at 67 MMT of which approximately 38 MMT are soybeans and 8 MMT domestic soybeans.

an imputed VAT of RMB 323, even though the analysis in Annex 1 shows that the effective VAT is 5.8 percent or RMB 155.¹⁴

After processing 1 MT of imported soybeans, the crusher's sales value (based on current market prices) are: 1) crude oil RMB 1296 and 2) soybean meal RMB 2028. The VAT sales receipt for the oil is RMB 149 or $1296 \times 0.13/1.13$. The VAT sales receipt for the meal is RMB 234 or $2028 \times 0.13/1.13$.

The crusher is liable to the Tax Bureau for RMB 60 VAT - the sales VAT minus the purchase VAT or $(149+234) - 323$. If the soybeans are domestically produced the VAT paid to the Tax Bureau is the same, but there is no purchase VAT receipt. The crusher retains the sales VAT but not collected by the Tax Bureau or RMB 262 ($323 - 60$). Based on this calculation, the effective VAT on soymeal is 5.75 percent.¹⁵ Other oilseeds are sold to feed mills tax-free.

Annex 4: Feed Millers

Feed sold does not include a sales VAT.¹⁶ The implicit ramifications on the domestic production of meat and its competitiveness with meat imports are discussed in Annex 5. The following analysis is based on the previous analysis and estimates the effective VAT on feed.

The import ratio of protein meal for feed millers is approximately 50 percent. The average ratio of grain to protein meal is estimated at 60 percent. On this basis, imports represent approximately 20 percent of inputs.¹⁷ Imports have an effective VAT of 13 percent. Grains, if purchased from the farmer and non-soy based protein meal, if the crusher purchased from the farmer, have an effective VAT of no more than 3.23 percent. Soy based protein meal has an effective VAT of 6.1 percent. The effective VAT will be grain \times 3.23 percent + imported soymeal \times 13% + domestic soymeal \times 5.75% + other oilmeal \times 3.23 percent. This is $60\% \times 3.23\% + 20\% \times 13\% + 5\% \times 5.75\% + 15\% \times 3.23\%$ or 4.845 percent.

Annex 5: Swine Farms and Slaughter Houses

Swine, poultry and cattle farms for VAT purposes are agricultural producers and therefore all sales are VAT-free. Imported meat products are charged a 13 percent VAT. The following analysis provides an estimate of the effective VAT on the domestic production of swine for pork production as an example of the VAT exemptions' impact on domestic Chinese meat production.

Post estimates that the material inputs (mainly feed and piglets) account for 75 percent of total production value and 85 percent of total production cost, respectively. Since no VAT is paid on inputs, the effective VAT to the slaughter house is the effective VAT for feed times the input ratio. This is 3.63 percent or 4.845 percent \times 75 percent.

For analysis of the effective VAT on slaughter house, an analysis similar that used for the crushing plant that is crushing domestic soybeans is appropriate.

¹⁴ Effective tax is purchase price $(2811) \times .0582/1.0582 = 154.6$.

¹⁵ Effective VAT rate = VAT / (PRICE - VAT) $180.79 / 2028 + 1296 - 180.79 = 5.75\%$.

¹⁶ State Administration of Taxation Notice (1999) No.39. Additionally, when feed mills purchase from a crusher, or other suppliers (e.g., mineral salts), the feed mills receive VAT receipts. As the sales by feed mills are exempted from VAT, technically, such purchase VAT receipts are useless to the feed mills. However, as VAT purchase receipts are legal documents identifying VAT paid, there is a known black market for these receipts for tax evasion purposes.

¹⁷ The only significant imported protein source is soybeans which is 20 percent of total inputs or 40% (protein component of feed) \times 50 % (import component of protein meal).

Assume the taxable value of 100 Kg of live pork purchased from a swine farm at RMB 800. The imputed purchase VAT is $800 \times 0.13 / 1.13 = \text{RMB } 92$. The effective purchase VAT is $800 \times 0.0363 / 1.0363 = \text{RMB } 28.02$.

After processing a 100 KG of swine, the slaughter house sales value (based on current market prices) is: 1) pork RMB 900 and by-products RMB 200. The sales VAT on the pork is $900 \times 0.13 / 1.13 = \text{RMB } 103$. The sales VAT on the by-products is $200 \times 0.13 / 1.13 = \text{RMB } 23$

The VAT paid by the slaughter house is the sales VAT – imputed purchase VAT or $(103+23) - 92 = \text{RMB } 34$. The effective VAT for the pork and by-product sales would be 5.97 percent.¹⁸ For the swine or pork imports, the VAT is 13%.

Annex 6: Import Tariffs

Import Tariffs of Hogs and Pork, Effective January-December, 2007					
		General	MFN	V.A.T.	Effective Rate
Live swine					(mfn+vat)
0103.1000	Pure-bred breeding Swine	0%	0%	13%	13.0%
0103.9110	Other swine, weighing less than 10 kg	50%	10%	13%	24.3%
0103.9120	Other swine, weighing 10 kg or more, but less than 50 kg	50%	10%	13%	24.3%
0103.9200	Other swine, weighing 50 kg or more	50%	10%	13%	24.3%
Pork					
0203.1110	Pork of sucking pigs, fresh or chilled	70%	20%	13%	35.6%
0203.1190	Other pork, carcass or half carcass, fresh or chilled	70%	20%	13%	35.6%
0203.1200	Hams, shoulders and cuts thereof, with bones in	70%	20%	13%	35.6%
0203.1900	Other pork, fresh or chilled	70%	20%	13%	35.6%
0203.2110	Pork of sucking pig, carcass or half carcass, frozen	70%	12%	13%	26.6%
0203.2190	Other pork, carcass or half carcass, frozen	70%	12%	13%	26.6%
0203.2200	Hams, shoulders and cuts thereof, with bones in	70%	12%	13%	26.6%
0203.2900	Other frozen pork	70%	12%	13%	26.6%
Source: China Customs					

Annex 7: Materials Input/Output Data

Production Value and Cost for Grains

Average Production Value for Grains (including Rice, Wheat and Corn) in 2005		
(1Ha= 15 Mu)	Unit	In 2005
Per Mu		
Production	Kg	393.10
Value in RMB	RMB	547.60
-Value for main products	RMB	529.48

¹⁸ VAT Rate = $\text{VAT} / (\text{PRICE} - \text{VAT}) = 62 (\text{feed VAT}-28 + \text{paid VAT}-34) / (1100 - 62) = 5.97\%$.

-Value for by- Products	RMB	18.12
Total Cost	RMB	425.02
-Production Cost	RMB	363.00
--Material and service input	RMB	211.63
--Labor Cost	RMB	151.37
---Cost for household labor	RMB	140.00
---Cost for labor employment	RMB	11.37
--Land Cost	RMB	62.02
Net profit	RMB	122.58

(Source: National Development & Reform Commission)

Average Production Cost on Grains (including Wheat, Corn and Rice) in 2005		
(1 Ha=15 mu)	Unit	In 2005
A: Material input and service/mu	RMB	211.63
Direct cost	RMB	203.62
1 Seed	RMB	24.90
2 Fertilizer	RMB	84.31
3 Household manure	RMB	9.03
4 Pesticide, herbicide	RMB	14.38
5 Film	RMB	2.01
6 Rental	RMB	63.26
On machinery	RMB	37.73
On irrigation	RMB	15.27
(for water)	RMB	6.57
On animal labor	RMB	10.26
7 Fuel	RMB	0.42
8 Technical consultant	RMB	0.09
9 Tools	RMB	2.60
10 Maintenance	RMB	1.63
11 Other direct cost	RMB	0.99
Indirect cost	RMB	8.01
1 Depreciation of fixed assets	RMB	4.49
2 Tax	RMB	0.74
3 Insurance	RMB	0.24
4 Management fee	RMB	0.76
5 Financial management fee	RMB	0.37
6 Sale Cost	RMB	1.41
B: Labor cost per mu	RMB	151.37
1 Pay for household labor	RMB	140.00
work days	Day	9.15
pay rate per day	RMB	15.30
2 Empolyment	RMB	11.37
Work days	Day	0.44
Pay rate per day	RMB	25.84

(Source: National Development & Reform Commission)

Production Value and Cost at Commercial Swine Farm

Production Value at Commercial Swine Farm in 2005		
	Unit	2005
Per Head		
Quantity of Main Products	KG	103.40
Total Production Value	RMB	814.52
---Value for main products	RMB	801.87
---Value for by-products	RMB	12.65
Total Cost	RMB	743.77
---Production Cost	RMB	741.20
----Material and Service Input	RMB	685.51
---- Labor cost	RMB	55.69
-----Household labor	RMB	33.97
-----Employed Labor	RMB	21.72
---- Land Cost	RMB	2.57
Net Profit	RMB	70.75

(Source: National Development & Reform Commission)

Production Value and Cost for Commercial Swine Farm in 2005		
	Unit	2005
Material Input and Service Cost Per Head		685.51
--Direct Cost	RMB	669.09
1 Piglet	RMB	211.33
2 Feed	RMB	408.00
3 Forage Feed	RMB	14.63
4 Processing fee on feed	RMB	4.55
5 Water	RMB	1.89
6 Fuel	RMB	5.44
-Electricity	RMB	3.21
-Coal	RMB	1.96
-Other Fuels	RMB	0.27
7 Quarantine fee	RMB	9.85
8 Looses	RMB	7.78
9 Technical service fee	RMB	0.60
10 Tools	RMB	1.73
11 Maintenance	RMB	2.14
12 Other direct cost	RMB	1.15
--Indirect Cost	RMB	16.42
1 Depreciation of Fixed Assets	RMB	9.73
2 Taxation	RMB	0.00
3 Insurance	RMB	0.05
4 Management fee	RMB	2.68

5 Financial Management fee	RMB	1.90
6 Sale Cost	RMB	2.06
Labor Cost per head	RMB	55.69
1 household labor	RMB	33.97
Work days	Day	2.22
Pay rate	RMB	15.30
2 employed labor	RMB	21.72
Work days	Day	1.07
Pay rate	RMB	20.30

(Source: National Development & Reform Commission)

Annex 8: Regulatory References

The following is an unofficial English translation of relevant VAT regulations or rules

1993/1994 State Administration of Tax Regulation "The Temporary Regulation of the VAT."

Article 2.

Item 2. The VAT rate for taxpayers selling or importing the following goods shall be 13 percent.

Part 1. food grains, edible oils

Part 4. feed grains, fertilizer, pesticides, agricultural machinery, agricultural plastic veneer

Article 4. The "payable VAT" is equal to the "sales VAT" minus the "purchase VAT."

Article 5. The "sales VAT" is the VAT collected by sellers from buyers when selling goods or providing services. "Sales VAT" equals the sale value multiplied by the VAT rate.

Article 8.

Item 1. The "purchase VAT" is the VAT paid by buyers when purchasing goods or receiving payable services.

Item 2. Except for items in 3 (below), the amount of the "purchase VAT" subtracted from the "sales VAT" shall be in accordance with the amount listed on the following documents:

A. VAT payment listed on the sales receipt provided by the seller;

B. VAT payment listed on the tax receipt issued by China Customs.

Item 3. Buyers purchasing VAT free agricultural products are allowed a "purchase VAT" reduction. The "purchase VAT" shall equal 10 percent of the purchase price.

* Effective 2002, the Ministry of Finance and State Taxation Bureau raised the purchase VAT rate to 13 percent from 10 percent. (See Ministry of Finance and State Administration of Taxation (2002) No. 12.)

Article 15. When tax payers import goods, the "payable VAT" is calculated according to the following formulas:

A. "Price for tax" equals clearance price plus tariff plus consumption tax (note: consumption tax on most commodity is zero with the exception for some luxury items, for instance, a 5% consumption tax on imported complete cars, or 8% for cars with a higher cylinder capacity)

B. "Payable tax" equals "price for tax" multiplied by the "VAT rate"

Article 16. The following commodities are VAT free.

Item 1. Products sold from agricultural producers.

State Administration of Taxation 1993/1994 "Implementation Procedures for the Temporary Regulation of VAT."

Article 31. The concept and scope indicated by Article 16, Item 1 of the VAT regulation is as follows: Agriculture includes planting, livestock, pasture, forestry, and fishery. Agricultural producers indicate either individuals or organizations handling agricultural production. Agricultural products indicate primary agricultural products and the specific scope is determined by local taxation bureaus directly under the State Taxation Bureau.

State Administration of Taxation Notice (2001) No. 30

Stipulates that soybean meal, regardless imported or domestically produced is subject to 13% VAT. For other meals, either imported or domestically produced is free of VAT.

State Administration of Taxation Notice (1999) No. 39

Article 3. The feed products sold to feed mills (commercial) farms and household farms are free of VAT.

Ministry of Finance and State Administration of Taxation (2002) No. 12

Buyers purchasing VAT free agricultural products are allowed a "purchase VAT" reduction. The "purchase VAT" rate is raised to 13 percent from 10 percent since 2002.

Ministry of Finance and State Administration of Taxation (2001) No. 113

Article stipulates that the following commodities are free of VAT

- 1) Agricultural plastic veneer
- 2) Fertilizer sale by the manufacturer (excluding nitrogen).
- 3) Wholesale or retailing on seeds, seedlings, fertilizers, pesticide, herbicide and agricultural machinery.